



## Rising Energy Prices May Still Have Long-Term Benefits

With gasoline prices on the rise again, there has been a public outcry over the rise in energy prices. However, there has been relatively little mention of the possibility that rising energy prices may actually have long-term benefits.

First, consider the flow of revenues from the sale of a barrel of oil. US dollars are given to the oil producers, predominantly OPEC member nations such as Saudi Arabia, Kuwait, etc. and non-OPEC nations such as Mexico, Norway, and Russia. Though countries such as Saudi Arabia and Kuwait enjoy a comparatively better standard of living than other OPEC members, developing countries should benefit greatly from the funds generated by oil exports by lifting the standard of living of millions of people in their nations in the long run. Mexico, for example, uses surplus oil revenues to fund infrastructure projects and to pay down debt. Norway's Petroleum Fund, with nearly \$200 billion in assets, will be used to pay the country's future pensioners. Though countries such as Venezuela and Iran have had their oil wealth hijacked by radical leaders pursuing anti-American policies and covert nuclear programmes, Iraq is likely to see substantial economic gains in the future as its new democratic government works to restore the oil infrastructure and increase the country's oil output.

Second, increased government expenditures in infrastructure projects (including reinvestment in the oil sector) in these oil producing nations will eventually aid economic advancement in those nations where the oil wealth is not being squandered by despotic leaders and should help to improve the lives of citizens in those countries. In addition, these infrastructure projects will likely need goods from industrialized countries, such as the United States, thus increasing trade for goods and services of companies that provide equipment and raw components used in infrastructure projects. These companies providing the equipment and materials may benefit in the form of increased earnings, which could in turn drive share prices higher and creates capital gains for investors.

Third, in the United States, the combined federal and state excise tax on gasoline averages roughly 42 cents per gallon, nationwide, and generated over \$58 billion in total taxes last year



(roughly \$1.4 trillion in aggregate since 1977). This may prove to be the fairest taxation of all, as those who spend the most pay the most. The owners of SUVs that get very few miles to the gallon pay the most in fuel taxes. Since the affluent travel more by most standards, they likely contribute the most to the government in the form of fuel taxes. The poor, particularly those in large cities who rely on public transport, bear a much lower proportion of this tax burden.

Fourth, rising energy prices have tested the endurance of the US and global economies, which seem to have absorbed the increased costs without any significant adverse economic impacts. Undoubtedly, some companies may initially experience a drop in earnings due to the higher fuel costs. However, all indications suggest that companies have adjusted their budgets to this increased expense. Increased energy costs may prompt management to become more efficient by exerting control over other expenses in an effort to improve the bottom line.

Fifth, the rise in energy prices from around \$33 per barrel in September 2000 to nearly \$70 per barrel in the wake of Hurricanes Katrina and Rita prompted President Bush and policy makers to call for an end to America's dependence on foreign sources of oil. America has long needed energy security since the Arab oil embargos in the 1970s. The current increase in prices may provide the impetus to pursue self sufficient energy policies such as increased exploration for domestic sources, the opening of the Arctic National Wildlife Refuge to drilling, or heightened research into alternative sources of energy.

Sixth, the rapid rise in gasoline prices following the hurricanes taught consumers a valuable lesson about the financial drawbacks of gas guzzling SUVs. In addition to a renewed interest in more fuel-efficient vehicles, alternative sources of energy have once again gained attention. Continued high energy prices could prompt increased investment in the production of fuel cells or ethanol and biodiesel, which could in the long run displace gasoline as the choice fuel for vehicles. An increased production of ethanol would, for example, be economically beneficial for America's corn farmers in the Midwest and sugarcane growers in Brazil. And, the trend towards more fuel-efficient, environmentally-friendly vehicles and less oil consumption would reduce emissions of greenhouse gases—a leading cause of global warming.



Finally, a move away from oil consumption could reduce revenues to certain oil-producing nations that may be hostile towards the west. This would deprive those hostile governments, some of which may sponsor terrorist organizations, of funds used in pursuit of nuclear programmes. An end to the west's dependence on foreign oil would also prevent hostile nations from ever using oil for economic terrorism.

Though oil companies may cringe at the thought of lower oil consumption and an end to their soaring profits, the energy companies could continue the trend of value creation for shareholders by embracing a shift away from fossil fuels as a primary source of energy and investing in renewable resources or alternative energy supplies.

Overall, there still appears to be a number of important long-term benefits to rising energy prices when considering the bigger picture. Perhaps we shouldn't complain so much. After all, we may be helping ourselves and future generations in the end.